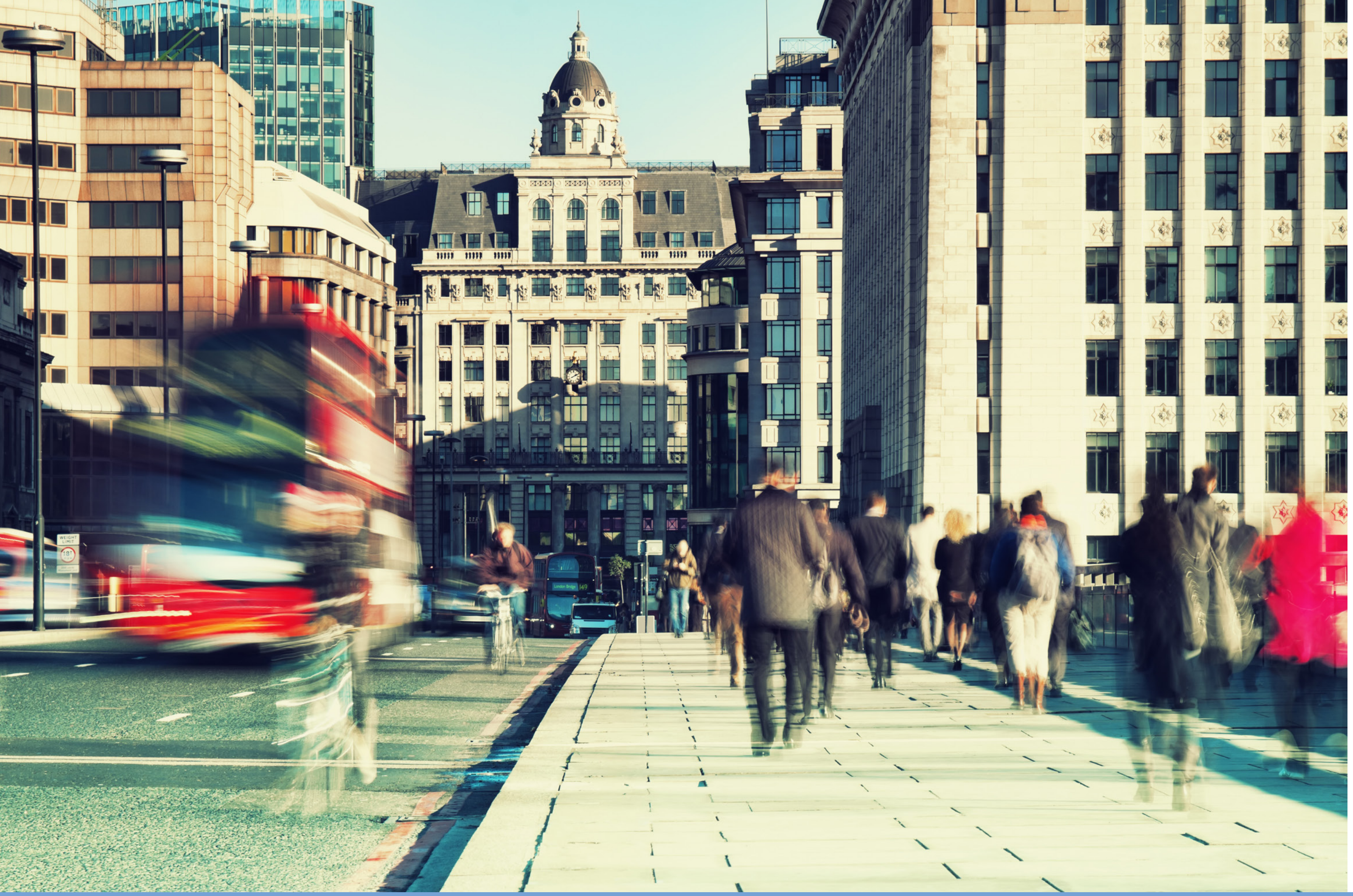
BANKING STANDARDS BOARD

ANNUAL REVIEW 2015/2016



Banking Standards Board

A NEW BODY FOR BANKING STANDARDS

The Banking Standards Board has been established to promote high standards of behaviour and competence across UK banks and building societies.

CONTENTS

CHAIRMAN'S STATEMENT
DAME COLETTE BOWE

The Banking Standards Board (BSB) was established in 2015 to help raise standards of behaviour and competence across the banking sector. Its existence reflects the recognition that, while effective regulation is vital for well-functioning markets, regulation is not – and cannot – be the answer to every question. Firms, and individuals within firms, have responsibilities that go beyond compliance. The way those responsibilities are met will depend on the norms, values, expectations, reward structures and role models, and the many other visible and invisible characteristics that shape behaviour in each firm – in other words, by a firm's culture.

The responsibility for culture lies with the board of each firm and with its executive team. It is a responsibility that extends beyond the level of the individual firm, to the sector as a whole.

Firms which join the BSB are making a positive and public statement about the responsibility of the industry to manage the culture of the banking sector, and of their willingness to work individually and collectively to raise standards and demonstrate trustworthiness across the sector. The BSB will support and challenge its members in their efforts, promote the sharing of good practice and new ideas, and report on progress or areas of concern.

This first annual review looks back over the work of the BSB's first few months, and ahead to its priorities for the coming year. These priorities reflect, in part, the themes that emerged from our first pilot assessment of ten firms in 2015. The assessment asked how each firm was performing against its objectives on behaviour, competence and culture, with individual findings provided to and discussed with each board. As the first exercise this is of course only a static picture – a snapshot. It is, however, an important starting point. Over time the annual assessment cycle and the evidence it provides will enable us to build a dynamic, comparative picture of progress or emerging concerns at both a firm and sector level; to benchmark firms against the rest of the sector or a part of it and to provide guidance on best practice and approaches that can help raise standards across the industry.

The themes from the 2015 assessment, and issues that we will explore further, are:

- **purpose, values and culture:** is a firm's purpose understood and 'owned' across the organisation? Are purpose, values and culture fully aligned, or are there in practice tensions between any of these elements, especially in stressed or uncertain environments?
- **culture and compliance:** how far does a firm's strategy for managing culture go beyond managing compliance and conduct risk? Is it focused on avoiding misconduct costs, or does it look more broadly at what influences behaviour and motivation across the firm?
- **leadership and key person risk:** strong leadership, and leadership by example, are key to a good organisational culture, but how does a firm ensure that momentum is not dependent on one individual? What is the role of the board in this, and of executive teams and middle managers?
- **incentive and reward structures and practices:** are these aligned with the firm's purpose, value and culture? What is the role of the Remuneration Committees in shaping culture? How does the firm manage the transition from sales targets, and manage any unintended consequences?
- **challenge and speaking up:** to what extent does a firm create and foster an environment in which staff feel free to speak up if something isn't right, or could be improved? What is the firm doing to encourage diversity of thought and experience within its workforce? How is this measured? and
- **the provision, take-up and effectiveness of staff training and support:** how are training and development used in practice? Is this consistent with the firm's objectives on culture? How is the impact of training on staff behaviour and competence, and ultimately on customer and client outcomes, measured? How does this inform future training?

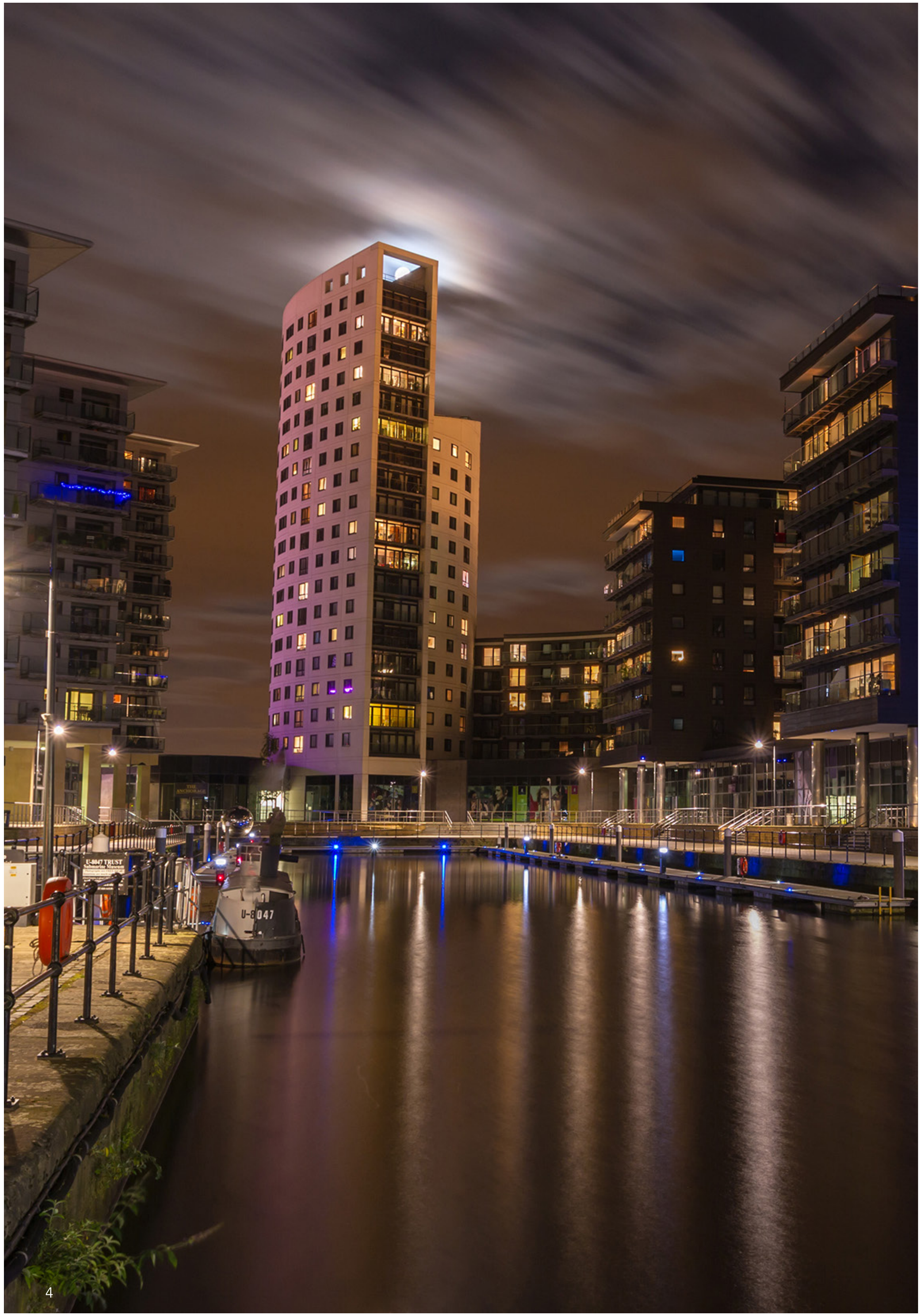
These are all big issues, and each will require coherent and concerted effort to address. The challenges for some firms on some issues will be greater than others – every firm's starting point is different – but the collective challenge for the sector is very large. Achieving it in a credible and sustainable way will be a long haul and a difficult one. But a start has been made.

The publication of this review is an opportunity to take stock of progress in our first year and to consider the implications of our pilot assessment for the approach we take with member firms in our second year and beyond. With our membership having opened at the start of 2016, it is also the right moment to report publicly on the work we have done and our priorities for the year ahead, and to invite challenge on and input to our efforts.

I am most grateful to all our Board members at the BSB for their many contributions to the Board's work this past year. And I would also like to thank Alison Cottrell, our CEO, and the executive team, who have got us to this point in a remarkably short time.

Colette Bowe

Dame Colette Bowe, Chairman



CHIEF EXECUTIVE'S INTRODUCTION
ALISON COTTRELL

The Banking Standards Board (BSB) is a small organisation with an ambitious remit: to help raise standards of behaviour and competence across the banking sector. As a non-statutory body working with the industry but not representing it, and with an expert and majority non-practitioner Board, it will develop and present an honest, impartial and evidence-based picture of culture, competence and behaviour in the banking sector. It will also help to change that picture, working both with individual member firms to assess how far they are meeting their objectives on culture, competence and behaviour, and with members collectively on professionalism, voluntary standards and the identification and dissemination of good practice and lessons learned from across and outside the UK banking industry.

Every bank or building society that joins the BSB is making a voluntary affirmation of its commitment to raising standards in the UK banking sector. This does not, of course, imply that all firms face the same challenges within their own organisation; each bank or building society will have its own culture, its own history, its own context and its own challenges.

Whatever their individual starting points, however, all member firms recognise a shared responsibility for managing the standing, reputation and trustworthiness of the sector; a collective trustworthiness that is not only important for customers, but that also has implications for the shape of regulation and the ability of the sector to attract talented people to work in it.

The BSB's role is to help, support and challenge its members in meeting both their individual and their collective responsibilities for culture, behaviour and competence, and we are using a range of approaches to do this. Our annual assessment exercise asks how far a firm's culture promotes desirable outcomes, what the board and the executive team are doing to achieve this, and how they know whether what they are doing is having any effect. In 2015 we piloted our approach with ten firms. This year we will build on and extend the exercise in a more systematic and comprehensive manner, and incorporate quantitative approaches that will begin to enable member firms to benchmark themselves against their peer group.

Alongside the assessment exercise, and working flexibly across firms and in collaboration with other organisations as appropriate, we are also focusing on promoting professionalism at all levels and in all parts of the sector; on exploring the relationship between law, regulation and ethics; on developing voluntary standards that will support a better service for customers; and on facilitating learning from within and outside the banking sector.

The BSB has come a long way very quickly since its launch in April 2015. It will maintain this momentum over the coming year, building on the work outlined in this first annual review to support and challenge the industry in its efforts to build trustworthiness and demonstrate credibly that it puts the interests of its customers and clients at the heart of its business. Only the industry itself can achieve this; not the BSB. It is no small task, and it will not happen overnight (or at all) without concerted and consistent effort; but it is an effort worth making. When staff working in banks and building societies across the UK can say not just that they are proud to work for their own firm (as many already are), but that they are proud to work in the banking sector, something will have changed.

Alison Cottrell

Alison Cottrell, Chief Executive

SECTION I
THE BANKING STANDARDS BOARD

The Banking Standards Board (BSB) is, as it publishes this first annual review, less than one year old. The factors that prompted its creation, however, date back to the financial crisis of 2008 and the failures of competence, behaviour, management and leadership – as well as breaches of the law – that were thereby exposed.

A succession of very serious issues in both retail and investment banking (including, but not confined to, the manipulation of the London inter-bank lending rate and foreign exchange benchmark rates, and the mis-selling of Payment Protection Insurance and interest rate hedging products) have damaged trust and confidence in the banking sector. While some of these practices stemmed from the period prior to the crisis, others occurred or continued well after it, notwithstanding conduct having risen up the agendas of bank boards and executive teams. The trust and confidence affected was that not only of customers, but also of taxpayers, regulators, public policy makers, investors and banking sector employees themselves. The challenge for the industry now is not to persuade its customers to trust it again; it is to demonstrate to these customers and to others that it is trustworthy.

Banking is not, of course, unique in having suffered a loss of trust in recent years, and examples of poor leadership and behaviour are not confined to the banking sector. Given, however, both the centrality of the banking industry to all our daily lives and the scale of the failures that occurred, the consequences of these breaches of trust were exceptionally damaging, costly and long-lasting.

A successful, dynamic UK economy needs a strong, stable banking sector that serves the best interests of its customers, both in the UK and globally. When confidence in the honesty, reliability and competence of the banking sector declines, the cost to individuals, society and the economy as a whole is very high; and while neither the crisis nor the breakdown of trust were confined to the UK, the relatively large size of the banking sector in the UK economy means that the ramifications of the crisis were felt (and continue to be felt) all the more strongly.

The events that precipitated and exacerbated the crisis have been extensively documented, in particular by the UK Parliamentary Commission on Banking Standards (PCBS). The PCBS recommended, in 2013:

> "work to establish a professional body should begin immediately as a demonstration that commitment to high standards is expected throughout banking and that individuals are expected to abide by higher standards than those that can be enforced through regulation alone. . . . A unified professional body for banking should have no need of public subsidy, either directly or indirectly. We would expect such a body to be funded by participating banks and individual qualified members. However, it would also need to establish independence from the outset, through its forms of governance, its disciplinary procedures and through the personnel at senior levels. The body must never allow itself to become a cosy sinecure for retired bank chairmen and City grandees. Just as importantly, it must eschew from the outset and by dint of its constitution any role in advocacy for the interests of banks individually or collectively[1]."

Following a careful examination of the options in his 2014 review of banking standards, Sir Richard Lambert concluded that there was 'a strong case for a collective effort to raise standards of behaviour and competence in the banking sector, and that the best way to deliver this [was] by setting up a new and independent body to drive the process forward'[2]. Membership of this new organisation would be open to firms – all banks and building societies in the UK – rather than to individual employees, though it would need to work closely with existing professional bodies. The Chairmen of six of the UK's largest banks and its largest building society[3] agreed to underwrite this proposal and translate it into action.

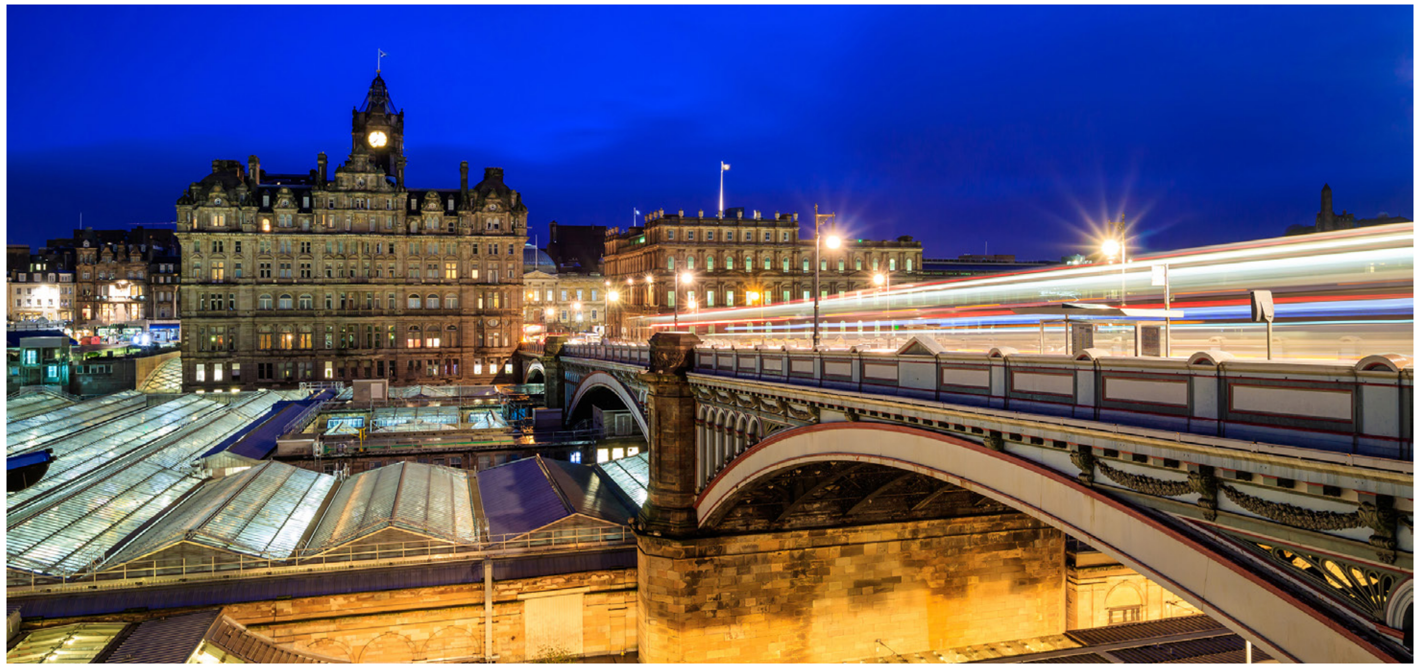
The aim was to create an entity focused not on encouraging customers and others to trust the banking sector, but on raising the *trustworthiness* of banks; a proposition that places the onus to act on firms themselves (rather than on their customers), and that looks across the whole spectrum of competence, behaviour and culture.

The responsibility for a firm's culture, behaviour and competence cannot be delegated by the firm to regulators or to anyone else; neither can it be confined within a firm to individual functions dealing with compliance, risk or human resources. It sits, first and foremost, with the board and the executive team. It is the boards of individual banks and building societies that take the decision about whether to join the BSB and publicly commit their firm to meeting this responsibility. The BSB's remit is, in this context, to help, support and challenge these boards and their executive teams, providing evidence-based information drawn from both a firm and sector level, and facilitating and encouraging continuous improvement and higher standards across the industry.

The BSB's Chairman, Dame Colette Bowe, was appointed by Bank of England Governor Mark Carney in November 2014[4] and its Board announced in April 2015. The new organisation opened its doors to membership across the bank and building society sector in January 2016.

The composition of the Board[5] reflects the BSB's remit. While the organisation is paid for, quite appropriately, by member firms[6], it exists to challenge the industry and raise standards across it. As such, the Board has a majority of members appointed from outside the industry and with the expertise to speak powerfully for the interests of those that the industry exists to serve. These non-practitioner members provide an assurance of the independent and impartial nature of the BSB's voice; one that will be used to speak about and with the industry, but not for it or on its behalf; the BSB has no lobbying mandate or capacity. The Board's practitioner members, meanwhile, are drawn from across the banking spectrum (and include also an investor perspective) to bring experience and knowledge of the challenges faced by the industry,

1. http://www.parliament.uk/documents/banking-commission/Banking-final-report-volume-i.pdf Changing Banking for Good, Vol 1, Summary, and Conclusions and recommendations (excerpts from paragraphs 94 and 96).
2. http://1984london.com/_banking-standards/pdf/banking-standards-review.pdf
3. Barclays, HSBC, Lloyds Banking Group, Nationwide, RBS, Santander, Standard Chartered Bank
4. http://www.bankingstandardsboard.org.uk/dame-colette-bowe-appointed-chairman-of-the-banking-standards-review-council/
5. See Annex for a list of Board members, or http://www.bankingstandardsboard.org.uk/meet-the-board/ for further details
6. Once completed, independently audited annual statements will be published on the BSB's website.



as well as a personal commitment to ensuring that the BSB fulfils its role of helping the sector improve standards.

The BSB is neither a trade association nor a regulator. It does not represent the industry, and it has no statutory powers. As a membership body, it takes the regulatory framework as a given and asks firms how they can not only meet the letter and the spirit of that framework, but also voluntarily go beyond it with respect to the wider issues of organisational culture that regulation either cannot, or is not best placed to, address.

As a private sector body with no statutory levers, powers of enforcement or lobbying mandate, the BSB has the flexibility to work across a sector that spans banks and building societies, foreign branches and subsidiaries, and retail and wholesale firms. We can, as appropriate, work efficiently and constructively with a range of organisations such as professional bodies, industry bodies, other industry organisations such as the Fixed Income, Currencies and Commodities Market Standards Board, academic institutions and professional networks. The BSB's structure, our ability to utilise advice and input from all sources, and the expertise and experience of our Board, all equip us to work in a creative, effective and efficient way. We will avoid duplication of what is already being done well, whether within firms or by other bodies, but will step in to inform, facilitate, challenge or disrupt and (equally importantly) step back again, as appropriate.

BSB membership is open to all firms operating in the UK with a banking licence. Membership is voluntary. Firms that join the BSB are making a strong, positive and public affirmation – to their customers, members, staff, investors and society as a whole – of their commitment to achieving high standards of behaviour, competence and professionalism, both individually and across the whole of the banking and building society sector of which they are a part.

The individual challenges and starting points for each BSB member firm will vary. For some, the challenge may indeed be about changing and improving their corporate culture. For other firms, it may be about sustaining standards, traditions and values in the face of changes in technology, markets, customer preferences, demographics or other external factors. For others still, it may be about aligning local, national and global cultures, or creating the 'right' culture in a newly established firm (or not losing that culture as the firm expands). Some challenges may be common to a number of firms, or across firms of a certain size, business model or market; but for each firm, the combination of challenges it faces, and that its board and senior executive team need to manage, will be as individual as the firm itself.

Whatever their individual circumstances, all member firms in joining the BSB are making a commitment not only to challenging and continuously improving themselves, but also to improving the standing and trustworthiness of the sector as a whole. This will take time and effort on the part of the firms involved. The BSB cannot achieve this for the industry; it can and will, however, help firms committed to achieving it, to do so.

The way in which the BSB is approaching this task over the coming period is outlined in the next two sections of this report. Section 2 describes the pilot assessment undertaken with ten firms in 2015 and sets out the key themes and findings that emerged from this initial exercise. Section 3, drawing on and informed by the themes from the 2015 assessment, sets out the BSB's priorities in 2016 and describes both the approach to the coming year's assessment cycle and the BSB's other work, including on professionalism.

SECTION II
THE 2015 ASSESSMENT

The rationale

The BSB's assessment work has two broad aims, one focused at the level of the individual member firm, and one at the cross-sector level:

- to provide individual boards with useable and relevant information that will help them judge the extent to which they are achieving their objectives with respect to culture, behaviour and competence in their firms; and to identify what is and isn't working, whether resources are being prioritised in the most effective way, and whether the objectives themselves remain the right ones; and
- to build up an evidence-based picture of developments across the sector that will facilitate collective efforts to raise standards, benchmark performance and share good practice.

There is little that is straightforward about culture, and no single 'good' or 'bad' culture that provides a template against which others can be ranked. Culture is a differentiating factor that can vary within as well as between organisations. It is hard to define, hard to measure, hard to manage and generally extremely hard to change, and certainly harder in each case than are compliance or conduct. The latter are often measured and managed in terms of the incidence of misconduct, as defined by regulation; there is, however, no word for 'mis-culture'. As difficult as it may be to pin down, however, firms cannot choose not to have a culture; only whether and how to manage it.

While there is no one template for a 'good' organisational culture, there are certain characteristics that we would expect such a culture in the banking sector to foster. These could include (but would not be limited to) a clear understanding of the firm's purpose and values; a relationship of respect and openness with customers, staff, members, investors, building society members and regulators; an executive team that genuinely leads by example; a focus on continuous improvement and professional development; a product design process that has the customer's needs, capabilities and best interests at its heart; high levels of employee engagement; effective succession planning; the fostering of internal challenge, feedback and 'speaking up' at all levels; and, of course, good conduct, and compliance with both the letter and the spirit of regulatory requirements.

A firm characterised, in contrast, by frequent regulatory breaches and incidences of misconduct, a reluctance to admit to or learn from mistakes, poor risk management, a lack of respect for customers and colleagues, an intolerance of different views or of people who didn't 'fit' a particular stereotype, a reluctance to seek and listen to feedback from around the organisation, or an inability at the top to recognise that what was happening around the firm was out of alignment with what the board assumed was happening, might also have a very strong culture and identity. It would, however, be difficult to describe such a firm as having a good banking culture.

The BSB's annual assessment process does not, therefore, assess a firm against a one-size-fits-all culture template. Rather, it asks how far a firm's culture promotes and fosters a range of desirable outcomes; whether what the board and senior team say they want to achieve on culture, behaviour and standards is consistent with what happens (and is seen to happen) at all levels across the firm; and how the board and senior team know whether what they are doing to manage and shape the culture of their firm is actually having an effect.

Following completion of the individual assessments, the BSB then draws together common themes from across all of the participating firms, identifying where possible good practices, sub-sector differences, emerging concerns, new questions or apparent gaps, in order to provide further information for member firms seeking to meet their commitment to raising standards across the sector. The lessons drawn from each assessment cycle will also inform the rest of our work and may suggest areas where, for example, formal standards or common metrics or benchmarks would be valuable.

The provision of a firm's assessment report is just one stage, albeit a very concrete and significant one, in an ongoing cycle. The report gathers together evidence and facilitates a conversation, but it is the board level discussion and the actions that follow that matter. We have, following the delivery of the 2015 assessment reports, been meeting with the boards of the participating firms. These discussions have been informative, constructive and challenging, covering both the findings of the 2015 exercise and looking ahead to 2016, and contributing further to our understanding of each firm and our ability to draw useful comparative conclusions.

The assessment approach

To help answer the questions set out above and to develop and refine the assessment process for the coming years, the BSB piloted an initial assessment exercise in the second half of 2015 with ten firms (the six banks and one building society that were the BSB's founders) and the additional three firms[7] that joined the BSB Board at the outset. This set of ten allowed us to test our approach on firms of different sizes, backgrounds, business models and markets, and – while recognising the constraints of the relatively small sample size – to begin to build up an evidence base of current practices across the sector with a view to being able to identify good practice, trends, divergent behaviours and gaps.

With the responsibility for culture, behaviour and competence lying firmly with the boards of firms and their senior executive teams, the BSB's assessment exercise is built around an ongoing dialogue with the Chairman, the board and the senior executive team of each firm.

The pilot exercise began accordingly with a short number of simple but stretching questions from the Chairman of the BSB to each bank or building society Chairman individually, asking:

- how would you describe the purpose of your firm, and the culture needed to deliver this? What are your priorities on culture, behaviour and competence over the coming twelve months, and beyond, and which do you expect will be the most difficult to achieve? How will you be measuring progress against your objectives?
- what have been the board's priorities on culture and competence over the past twelve months and why? How have you gauged the effectiveness of the steps taken to develop and embed your firm's culture, and where has most/least progress been made?
- how confident are you that management and staff at all levels across the organisation live and exemplify the firm's values? How do you know this? and
- what outcomes and behaviour does the board seek to incentivise for your firm's staff, and through what means? What are the objectives and reach of your Remuneration Committee? How is this intended to support its purpose and influence culture and behaviour at all levels in the firm? What effect has it had to date on culture and behaviour, and what evidence do you use to gauge this?

These questions were designed to help us understand each board's priorities and concerns, and its current approach to culture, behaviour and competence within the firm. The answers allowed us to begin to identify themes, similarities and differences across our sample of firms. For each individual firm, the challenges identified by the board as priorities in 2015 will provide a helpful starting point against which to judge progress in the 2016 assessment exercise.

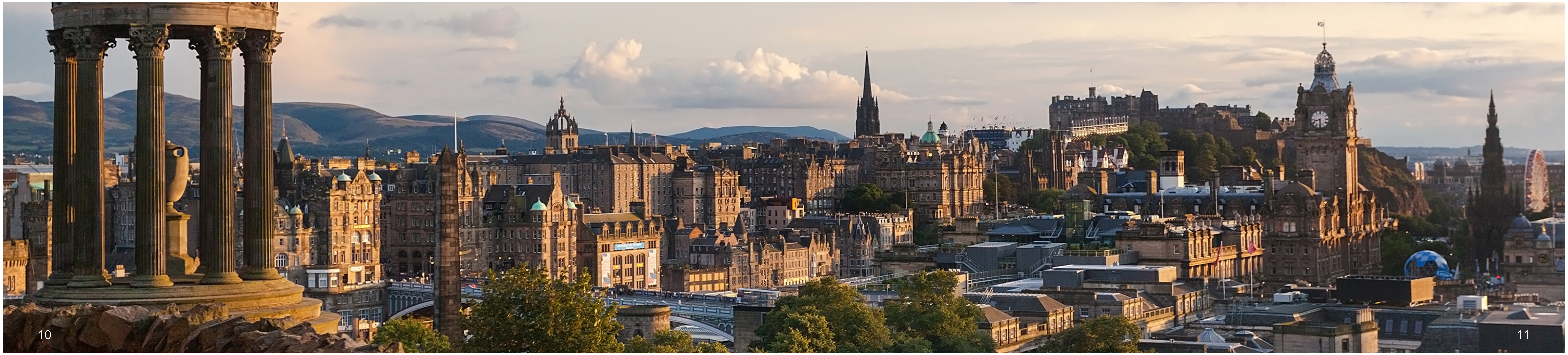
[7] Citi, Metro Bank and Morgan Stanley.

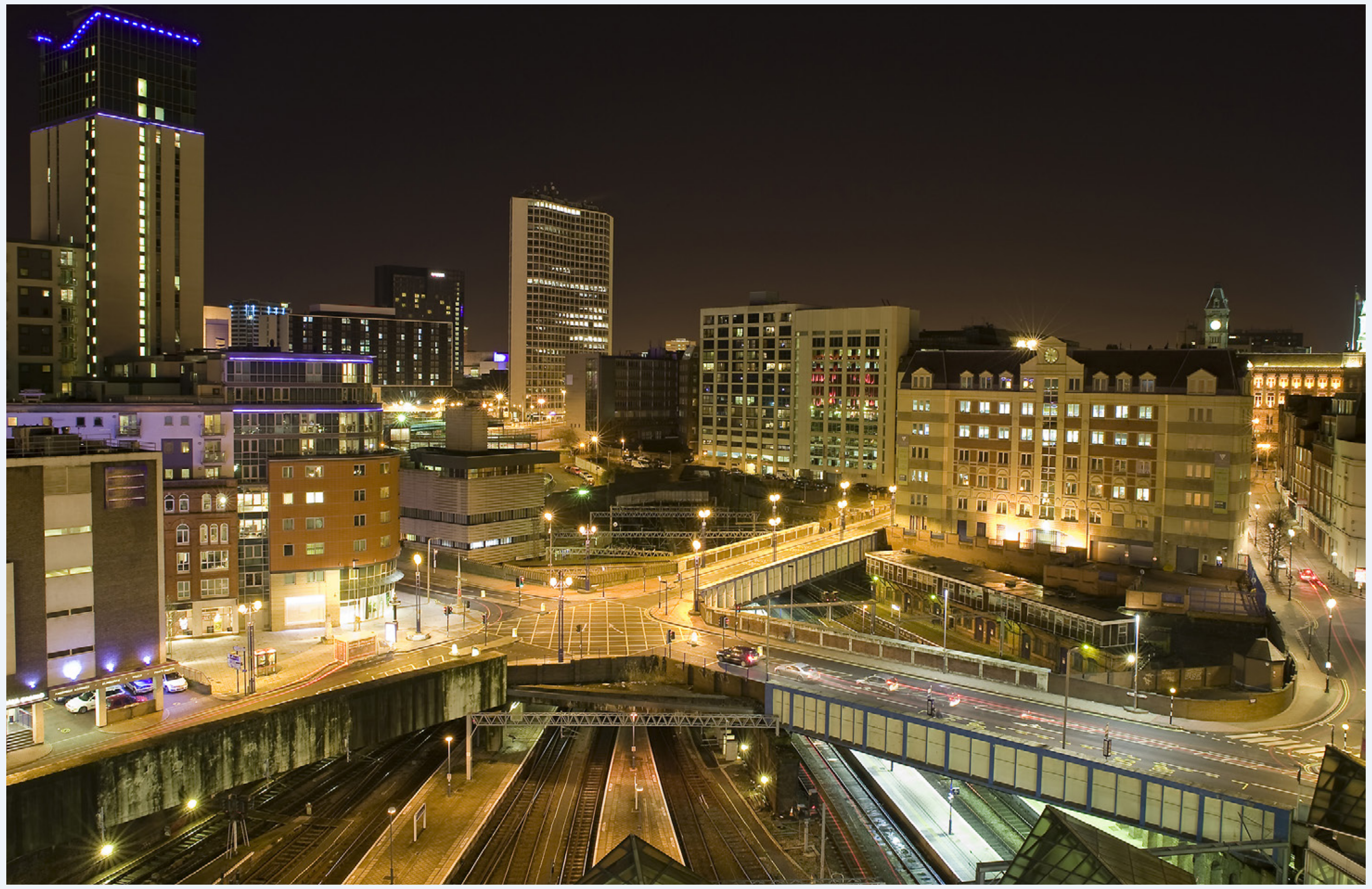
Alongside the questions sent to the Chairmen, we asked a number of factual questions of each CEO. These were intended to help give us a sense of the processes and approaches the firm already had in hand with respect to, for example, training and development, hiring, promotion and diversity, as well as how the executive team already measured staff engagement, communicated with employees and sought to assess and manage culture, behaviour and competence. The aim in each case was to help us to understand what the firm was already doing, what information each board was receiving to help it set strategy and priorities and monitor performance, and what was (or wasn't) common practice across our ten firms and potentially across parts of the sector more broadly.

We also tested these themes with junior and middle-ranking staff. Timing and practicalities – given that the BSB itself only came into being in the second quarter of 2015, so the 2015 assessment exercise had effectively to be initiated and completed within a six-month period – meant that our focus groups and 1:1 interviews were not large enough to be fully representative of each firm's workforce. The results, nevertheless, were insightful and, alongside informal input from investors, trade unions, consumer groups and others, informed the reports sent back to firms at the turn of the year and the subsequent discussions with each board.

As noted, the objective of the assessment is not simply to deliver a report; it is to equip boards with information and perspectives that will enable them better to provide leadership across all those areas that feed into and shape the culture of their business. The discussions that the BSB has been having with each Chairman and board about their firm's 2015 report have been central to the exercise and key to ensuring that the assessment work is both useful and used.

The BSB sent the findings of each individual assessment exercise to the board of the firm concerned. Each board owns its report, and it is the board's responsibility as to whether and how it disseminates its contents, internally or externally. The BSB has not published and will not publish firm-level findings. It will, however, draw together each year the themes that emerge from across the individual assessments and report on these. The key themes from the 2015 assessment are set out in the section that follows.





Key themes

As well as the firm-specific information contained in each report, the assessment exercise also aims to identify any generic themes and approaches that may be of value across member firms and to the sector collectively. The constrained nature of the 2015 assessment exercise and the non-random nature of the ten firms that participated, mean that the results of the pilot cannot be regarded as representative of the banking landscape as a whole, or indeed of any individual firm. Furthermore, given the partial nature of the evidence base, the emerging themes reflect in some cases our interest in finding out more about issues on which relatively little information was available or provided. Notwithstanding this, however, six themes emerged from the exercise that may merit reflection from banks, building societies and others, and that have informed the BSB's future work plans.

These themes, described below in more detail, comprise:

a. the alignment of a firm's purpose, values and culture

b. the difference between a focus on culture, and on compliance

c. leadership and key person risk

d. incentives and reward structures and practices

e. fostering challenge and speaking up

f. the provision, take-up and effectiveness of staff training and support

a. Purpose, values and culture

Firms varied in terms of their statements of purpose and how they set these out. Some, for example, referenced explicitly their role in society; others did not. Within the small workforce samples we surveyed, staff varied in the extent to which they said they identified with the values set out by their firm.

We were particularly interested in whether a firm's purpose and the values it espoused were clearly articulated, understood and perceived by staff to be aligned with the firm's business model and practices – whether the firm's culture and values were intrinsic to its purpose and strategy, or whether they were 'add-ons' and, as such, vulnerable to being forgotten or subsumed if the firm's business strategy or bottom line came under pressure.

Underpinning this was an assumption – and one that we will test – that an organisation that is clear about its purpose and that has a culture and values that reflect and are consistent with its purpose, will be one in which staff are able to feel confident that there is no conflict in principle between what they are expected to do and how they are expected to do it. There would be no mismatch between the pressure to perform and the pressure to behave. A lack of alignment between purpose, values and culture could, in contrast, give rise to stress and uncertainty among staff trying to second-guess what takes priority in any given situation, as well as a lack of engagement with what might be regarded as the non-strategic side of the business agenda.

Aligning purpose, values and culture is not always straightforward even in a small or relatively simple firm. For a large, complex or global firm in which aspects of culture may vary within the organisation, ensuring that culture in each part of the group is consistent with the firm's overall purpose and values can be even more challenging. It was not always clear from our exercise how cultural variation within firms – whether across geographies or business units or functions – was understood and, as appropriate, managed, reduced or fostered. Without recognition and discussion of intra-firm cultural variation, a pre-requisite for which is having information at a level of granularity that allows such differences to be identified, boards and executive teams cannot adequately assess the risks stemming from differences across their organisation or, more positively, take advantage of opportunities to learn from different parts of the business.

b. Culture and compliance

Culture is different from compliance, though the two concepts tend to be used interchangeably (and with 'conduct' often standing in as a synonym for both). Equally, however, they are not independent of each other; one characteristic of a good culture in the banking sector will be high levels of compliance and conduct, but 'culture' itself is much broader than this. The culture of a firm will shape the way it approaches regulation and the way it complies with regulation. There is a world of difference between a firm that focuses on the outcome a regulation is designed to achieve, and a firm concerned primarily with avoiding conduct breaches at least cost.

Firms frequently used the word 'culture' during their assessment. It was, however, clear that different firms meant different things by this. For some, the focus was in practice primarily on understanding and mitigating conduct risk. Some others, in contrast, had explicitly identified a need to change aspects of their culture more broadly, and were clear as to the reasons for this change (though sometimes found it easier to describe the culture they aspired to or that they felt that they had moved away from, than the culture they currently had). Others, meanwhile, reflecting the different starting point and experience of each firm, were concentrating on maintaining or building on their existing culture rather than changing it.

Where failures of compliance and of culture had occurred in the recent past, firms also differed in the extent to which they appeared to recognise and 'own' responsibility for this. We will be interested in exploring how organisational openness about what went wrong and why, and being clear about why this matters for the whole of the business and not just for a part of it, contributes to the credibility and effectiveness of efforts to move away from the behaviour and culture that produced those failures. It will also be interesting to observe over time whether a readiness to acknowledge responsibility in this way is correlated with the success of efforts to encourage speaking up and accountability at an individual level with staff.

The variety of approaches used by firms to help them assess their current culture or culture change, and to understand the external (customer) and internal (employee) implications, are described in Figure 1.

FIGURE 1:
Measuring culture and cultural progress – range of approaches used by firms

STAFF ENGAGEMENT AND CULTURE SURVEY

Most firms use annual staff engagement surveys, supplemented by separate culture and climate surveys or modules added to the regular engagement survey

CUSTOMER PERCEPTIONS AND OUTCOMES

Some firms see the real test of culture as being in the outcomes it generates. They focus in particular on customer satisfaction scores, with some going further to try and test outcomes (eg, mystery shopping or regular online panels of customers)

INDICATOR DASHBOARD

Several firms use a range of indicators, sometimes consolidated into 'culture dashboards', including:

- Customers: satisfaction scores, Net Promotor Scores, complaints
- Employees: engagement scores, speaking up scores, turnover, absence rates, grievances, use of whistleblowing lines
- Conduct and risk: conduct breaches, clawbacks, material events and escalations

VALIDATION

A range of methods is used by firms to validate their progress or performance and confirm their understanding:

- Consultancy firms' benchmarking exercises
- Other external benchmarks
- Internal Audit assessments
- Triangulation across various data sources, eg, staff and customer surveys

C. Leadership and key person risk

The importance of key individual leaders (often CEOs) to changing or maintaining corporate cultures was identified by staff in a number of the firms that we assessed. While individual leadership is key to success, and nowhere more so than on an issue as difficult and entrenched as culture often is, it brings the risk that the momentum behind and commitment to that programme becomes associated very personally with that individual. When, as will inevitably be the case, that person moves on, some of the momentum and commitment may be lost with them, and the challenge for their successor be all the greater.

The answer to this is not for CEOs or other leaders in a firm to exhibit fewer of the leadership skills that have contributed to their success. Strong inspirational leadership is precisely what is needed to initiate and promote cultural change, and the 'key person risk' identified here is a product in part of success. What is important is that, over time, the responsibility for managing and safeguarding the firm's culture becomes shared; by the board, the executive team, and across the entirety of the firm itself. A culture that is contingent on the presence of a specific individual cannot be described as the culture of the firm; the latter will be what resurfaces once the key individual has moved on.

Our assessment work and subsequent discussions have underlined the importance of the active support of the Chairman and the board to the effectiveness of programmes intended to change or maintain culture. There were also indications of some boards placing increasing weight on culture as a factor in succession planning, to ensure continuity of focus and leadership skills.

While the example set by the executive team and the board is a crucial determinant of a firm's culture, it is not, however, sufficient in itself. Culture in any part of a firm will be shaped also by the expectations and behaviours of immediate managers and colleagues, and by local role models. Some firms have started to focus on middle managers as a critical group of staff to talk with, listen to and engage, and are now more actively involving managers below the most senior levels in implementing cultural programmes. Figure 2 describes some of the approaches that different firms use, both in communicating the 'tone from the top' and in engaging staff at all grades.

FIGURE 2:
Communicating values and behavioural expectations to staff

PROVIDING CLARITY ON VALUES AND BEHAVIOURAL EXPECTATIONS

- Face-to-face learning or 'off-sites' at which culture is explicitly linked to strategic aims and managers have the opportunity to explore ethical dilemmas in a practical way
- Leadership development programmes which incorporate a clear articulation of behavioural expectations
- Support for line-managers in explaining and implementing strategic and cultural priorities, recognising the pressures faced by staff in middle management grades in particular

PERSONALISED COMMUNICATION FROM LEADERS

- Regular email and intranet updates from the CEO
- Q&A phone sessions with the CEO
- Video diaries from executive team members

INTERACTIVE METHODS

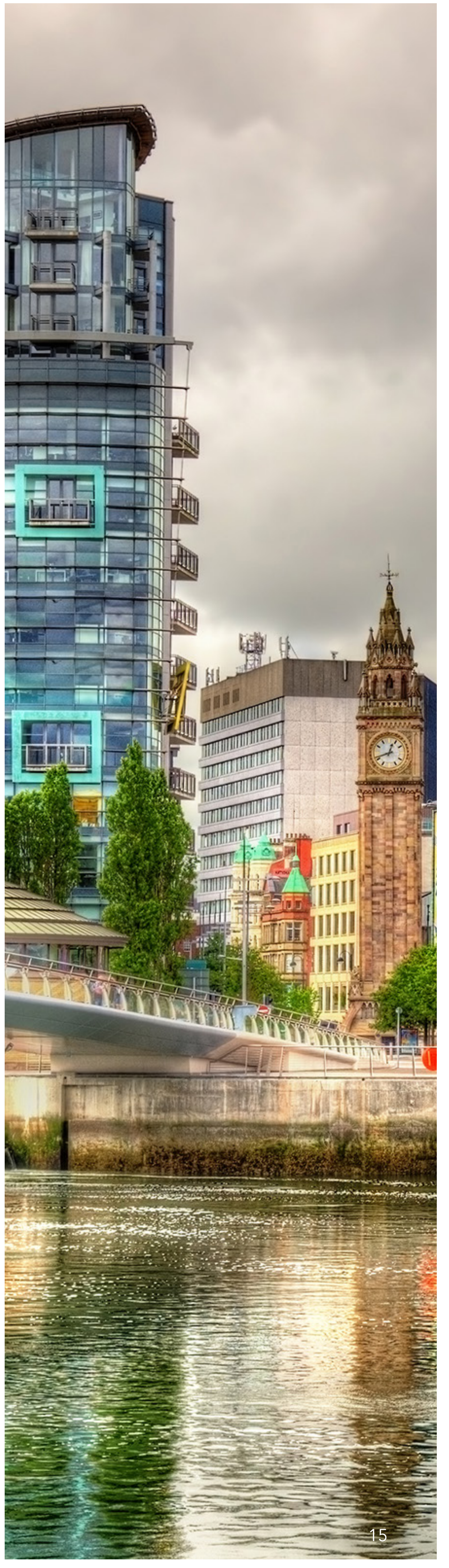
- Collaboration sessions via internal social media platforms
- Regular leader-facilitated meetings, discussion-based breakfasts and events for staff

ORGANISATIONAL MEDIA

- Formal memorandums and bulletins
- Use of the intranet
- Use of employee magazines
- Digital screens in lobbies
- Regular e-learning
- Promulgation of decision making tools

CASCADE PROCESSES

- Cascade from leadership team to managers and then to employees
- Monthly team briefings to help managers communicate key messages
- 'Town Halls', roadshows and other events
- Employee-led networks



d. Incentive and reward structures and practices

The issue of bankers' pay has rarely been out of the headlines since the financial crisis. This is of course also true of pay in other sectors, but the context of taxpayer support for the sector during the crisis, a continuing legacy of misconduct (not all of it pre-crisis), and a perceived lack of individual accountability for failure or wrong-doing, has made the issue particularly contentious within banking.

Remuneration and reward structures play a crucial role in aligning behaviour with a firm's values and purpose. As such, they feature prominently in the BSB's work, whether in the context of the assessment exercise or other themes or projects. Given the diverse nature of the sector and the different environments that different firms, or parts of firms, operate in, it is helpful to approach this topic from two perspectives; first, the remuneration of senior executives and material risk-takers (the latter, in particular though certainly not solely in the investment banking sector); and second, pay and incentive structures more broadly, covering the bulk of banking sector employees.

Executive remuneration – its scale, structure, cost and rationale – has come under increasing scrutiny in recent years from a range of sources. The regulatory focus has encompassed the scale of remuneration, its composition and the terms and timing of variable pay. The result is a pay structure for senior staff and risk-takers that is now more constrained. It remains, however, open to challenge, with early 2016 seeing some senior figures in the industry commenting publicly on the merits and costs of established pay practices, in particular in the investment banking sector.

Executive remuneration is clearly relevant to any consideration of culture in a firm or in an industry. Firms have been adapting to and implementing a wide range of national and global regulatory initiatives, and the full impact of these remains to be seen. We will be paying close attention in our continuing assessments to the way in which firms take responsibility for ensuring that executive and risk-taker remuneration structures and processes are aligned with the stated purpose of the business, and to how this is communicated. The role of Remuneration Committees in setting bonus conditions and targets will be an area of particular focus.

Financial incentives do not, however, apply to and affect the behaviour of only the highest paid staff in an organisation. They also play a powerful role in shaping the culture at all levels, including in front-line positions. In the 2015 pilot assessment, we explored the extent to which remuneration structures throughout the firm – below the senior tier, and encompassing customer-facing staff in the retail and commercial banking sectors – were aligned with what the firm set out as its purpose, values and culture. Given that reward structures in the retail and commercial sectors are more likely, for most staff, to be set in a 'top down' manner across a whole firm; the changes in behaviour they incentivise can have very large consequences, as past mis-selling scandals demonstrate.

Firms have in general been changing performance assessment and remuneration practices. They have moved in many cases towards balanced scorecard approaches or assessment mechanisms that give a greater weighting to behaviour.

In many retail banks, aggressive sales targets appear to have been removed or softened. This has produced a lack of certainty in some cases among staff and managers as to how performance is in practice now measured. Ensuring that managers understand the new approaches, and that sales targets do not reappear via the back door or at local level (either because of confusion over the new approach, or if pressures build on the bottom line), will be challenging.

The extent to which firms see (or indeed are looking to identify) changes in behaviour stemming from changes in remuneration practices, is less clear. There is a question in this context about the role that Remuneration Committees might play in considering the influence of remuneration structures, and of changes in these structures, on the firm's culture. It also suggests a further area to explore, in terms of how far the role of the Remuneration Committee is joined up with those of other board committees focusing on culture or conduct. If a Remuneration Committee does not factor culture into its thinking, culture is unlikely to be intrinsic to the way that a firm pursues its business.

FIGURE 3:
Performance assessment mechanisms

MOST PRESCRIPTIVE	LEAST PRESCRIPTIVE
Balanced scorecards with defined weightings for behavioural elements Performance is assessed against a specified balanced set of objectives. These often include customer and colleague feedback, adherence to appropriate risk management processes, behaviour that is in line with values, and performance against agreed business/ financial objectives. Outcomes are often subject to 'moderation' and challenge **Example** An explicit 50/50 weighting between behaviours (the 'How') and business performance (the 'What'). Business performance is further broken down into specific financial and non-financial targets	**Discretionary approach** A non-scorecard approach where staff are assessed on the basis of individual, group, and business performance, and management of risk. The process relies on manager discretion **Example** A line manager assesses the performance of an individual based on what has been delivered during the period, taking into account whether this individual has met the behavioural standards expected. Performance scores may be reduced to reflect incidents of poor behaviour during the year

FACTORS TO CONSIDER

Do specific measures have any unintended consequences for behaviour? What is the most effective weighting for behavioural elements in balanced scorecards?	How confident do managers feel in being able to make these judgements? Does the use of discretion imply a lack of clarity or transparency in how individuals are rewarded?

How to communicate to staff that failure against the 'How' has in practice had a material impact on reward or promotion, without identifying individuals?

GUIDANCE ON ASSESSING BEHAVIOUR

In many cases, guidance is provided on assessing behaviour for staff having or holding performance assessments. Typically, this describes desirable and undesirable behaviours in line with the firm's values

e. Challenge and speaking up

Challenge and speaking up was a theme common to many firms; it is also one that can encompass a range of issues. At one end, it may be about awareness of and confidence in the firm's whistle-blowing arrangements; at the other, about the extent to which a junior member of staff feels able to say that he or she has a better idea about the way in which something might be done.

Firms focused to different degrees on different parts of this spectrum, but appeared to be consistent in their wish to foster an environment in which staff would challenge and speak up when poor behaviour was observed; when actions were being considered that would not be in the customer's interests or aligned with the firm's values; when decisions already taken were having unintended consequences; or when something could be done in a better way.

The extent to which staff are willing to speak up and challenge will depend on their confidence both that doing so will not have adverse consequences for them (or their colleagues), and that if they do speak up, something will be done as a result. To promote a culture in which speaking up and challenging is normal, organisations need therefore not only to encourage it but to respond to it, and to do so very visibly.

Diversity of thought, experience and approach may also be important in creating an environment in which challenge and speaking up are the norm. When most people approach an issue from the same perspective, the minority views may be more likely to go unvoiced. The importance of actively fostering challenge and different views may, paradoxically, be all the greater in a very 'friendly' working environment, as staff may feel more constrained in speaking out or going against the grain where working or social ties are very strong.

There is, of course, a balance to be struck between strengthening the culture 'fit' of a team or workforce and ensuring that challenge or difference is encouraged, and there is no one right answer. Hiring at any level is, however, a key part of managing that fit, and a firm's hiring policies will be a central influence on and reflection of its culture. Figure 4 describes some of the different approaches used by firms.

Diversity, for some firms, appeared to be considered primarily in terms of legal requirements and protected characteristics and, to some extent, external expectations, rather than seen as integral to a firm's culture, purpose and strategy. This is surprising, given the numerous potential benefits of diversity of experience to a firm's business goals (eg, enhancing its ability to identify and manage risk, encouraging aspiration among its staff, attracting talent from across the workforce, retaining staff, relating more effectively to its customers and the society it serves, and encouraging the expression of different points of view or perspectives).

The stated diversity focus of most firms is almost exclusively in relation to gender, and to a lesser degree on ethnicity and/or sexual orientation. Firms used different quantitative measures, making comparability difficult. Targets (primarily for gender) tend to be focused at senior level representation rather than extending to the pipeline that feeds internal promotion to those senior positions.

A broader concept of diversity and a more transparent approach to measuring success, and one more clearly rooted in the firm's own purpose and business interests, would help many firms improve their effectiveness in fostering the culture that they are working hard in different ways to create.

f. Staff training and support

Firms in general have a wide range of training and development material available for staff, and policies that encourage them to use it. The overall culture of a firm may not, however, be so supportive in practice of these training opportunities actually being taken up. It may also not foster efforts to assess the efficacy of the training received. The impact on behaviour and norms of each member of staff receiving induction or refresher training in ethical behaviour is, for example, likely to be different where this involves a peer group discussion using real-life scenarios and dilemmas, to where it comprises a short online package completed by the individual at their desk, even though both might tick the box in terms of training having been provided.

Many firms provide decision-making tools that employees can use when faced with difficult judgements or ethical dilemmas. The assessment suggested that, where these tools are clear, and in particular where they nudge individuals towards taking into account personal considerations in their judgements, staff both use and value them. In contrast, staff are less inclined to use overlapping and more complex tools that require more abstract judgements. Understanding this dynamic through further investigation will be important to evaluating the effectiveness of the approaches used by firms. The type of training offered and its take-up are, of course, just the first steps. The next is to assess the actual impact on decisions of using such tools, to help assess their effectiveness.

Staff frequently described their working culture and environment as fast paced and intense; a finding not only in investment banking samples, but also in some corporate and retail banking functions. Such words can, of course, have positive and negative implications, and need careful contextual interpretation. The adverse implications in terms of increased prolonged stress levels and wider detrimental impacts on the health of employees make this, however, an important area for detailed consideration. Given that stress can affect how people weigh risk and reward, and therefore the way in which they make decisions, it is important from both a duty of care and a business perspective that staff wellbeing and health are incorporated within firms' cultural agendas, both as an input and influence on actions and behaviour, and as an outcome.

FIGURE 4:
Recruitment practices and priorities

CULTURAL FIT ⟷ CAPABILITY

Prioritisation of cultural fit	Balance of capability and cultural fit	Prioritisation of capability
Selection primarily designed to determine cultural fit; skills are a secondary factor. For many roles, training is provided once the right person is selected, and processes are designed to reduce the specialism required at junior levels **Example** A firm does not allow the hiring of a full team from a competitor, or a new hire to bring in ex-colleagues, because the result may be to import a culture that does not align with that of the firm	Selection based on competency (role-specific skills and knowledge), expected behaviours, and cultural and motivational fit	Selection primarily based on capability, skills and experience. Candidates assessed against criteria such as judgement, drive, influence and execution. Reliance on background checks as main indicator of ethical conduct **Example** A firm permits the hiring of a full team because it provides the required expertise

FIGURE 5:
Diversity

HIGH FOCUS ⟷ LOW FOCUS

Gender	Ethnicity Sexual orientation Disability	Age Carers/ Parents Ex-military	Other e.g. socio-economic Religion

Diversity targets

Most firms have targets for gender representation at the top levels of the organisation (either at board level or senior management level). For those that have targets, these are typically about achieving between 25%-40% female representation in the most senior roles over the next 3-5 years

Integrating diversity into operations

Many firms use their internal diversity groups to help integrate diversity into their operations, and extend their approach externally to customers or suppliers

Example 1
A firm engages its staff disability network to trial new processes for customers with a disability

Example 2
A firm shares its best practice findings with its suppliers to promote diversity beyond the firm itself

SECTION III
NEXT STEPS: THE BSB'S WORK IN 2016

The BSB's work in 2016 will be informed by the key themes that emerged from the 2015 assessment (described in the preceding section) and the subsequent and ongoing discussions with boards and executive teams of the participating firms, as well as by the BSB's wider engagement with other organisations, groups and parts of civil society. It is also important that this engagement takes place across the UK and not just in one part of it, and the BSB will be following on from its successful visit to Birmingham in October 2015, and a very helpful series of discussions, with further visits over the coming months.

Discussions with participating boards of the 2015 assessment reports confirmed the validity of the themes identified, and highlighted some as being of particular current interest to a number of firms (such as speaking up and training). They also underlined the shared priority attached to finding better ways to measure outcomes and benchmark performance.

While the assessment exercise is a core element of the BSB's work, it is far from its entirety. In 2016 the BSB will also complete and build on projects already initiated, including on professionalism, on the Certification Regime and on law, regulation and ethics. The conclusions of these projects (or of their first phases) will themselves inform subsequent priorities and the shape of ongoing work.

The BSB's approach to addressing all of its work will remain one of working flexibly, collaboratively and efficiently throughout, avoiding duplication and working with and through partners as appropriate while retaining independence and impartiality. This is particularly important with respect to standard setting. Success will be defined not by the number of BSB standards set in any one year, but by the value, relevance and usefulness to customers of the standards set. Where an appropriate standard already exists under the auspices of another organisation, we will not duplicate that work (though we may support it). Equally, where a gap exists and we consider that a voluntary standard would be of benefit, we will consult on and take forward that work.

The key areas of work, described in more detail below, include:

- designing and undertaking the 2016 assessment exercise, building on the 2015 pilot and scaled up to include a wider number of member firms, informed by the key themes identified in 2015;
- promoting professionalism across all parts of the banking sector and at all levels;
- exploring the relationship between law, regulation and ethics, and what this means in the specific context of banking and banking culture; and
- developing voluntary standards that will support a better service for customers and other relevant parties across the sector.

In addition to these areas of work, the BSB will continue to foster and facilitate learning from within and outside the banking sector via its series of breakfast seminars, conferences, UK-wide visits and other member events[8].

The 2016 agenda will be kept under review and adjusted as needed to ensure that it remains relevant, timely and appropriate, and that it is undertaken as effectively and efficiently as possible.

[8] Details of past and forthcoming BSB events can be found at http://www.bankingstandardsboard.org.uk/events-programme/

Assessment

An important part of the BSB's work in 2016 will be to develop the assessment approach and extend it across a wider number of firms. All BSB member firms with a legal entity domiciled in the UK are eligible for an assessment. Smaller firms, for whom an annual exercise may not always be appropriate, can choose to opt in to the assessment exercise in any given year. Given the centrality of direct board engagement to the assessment, firms that operate in the UK as a branch and have their headquarters overseas are not currently eligible for the full assessment exercise (though as outlined further below, will be included in the survey element).

The 2015 assessment was, as has been noted, a pilot exercise conducted with ten firms. In 2016, the first year in which the BSB has been open to membership, the assessment will be open to all eligible member banks and building societies.

Last year's assessment was primarily a qualitative exercise based on boards' and senior executives' response to our questionnaire, and focus groups and interviews with small samples of staff. The exercise by its nature required subjective judgements and, because it was based on small sample sizes, the findings from the staff engagement were not statistically representative.

In 2016 the assessment exercise will be both more systematic and more comprehensive. It will cover a greater number of firms and, very importantly, will develop and incorporate quantitative approaches aimed at enabling firms to benchmark themselves against their peer group. It will adopt techniques to enhance our understanding of what influences behaviour, and incorporate the views of (and take into account the effect on) a wider population of the sector's stakeholders. This wider group includes customers, representatives of civil society and (for banks, though not building societies) institutional investors – the latter, a potentially important influence on the behaviour of the firms they own and invest in.

In designing the 2016 assessment we have been working with selected external partners from a leading consultancy firm, as well as with academics from the London Business School and the London School of Economics. We are also continuing to engage with and learn from a wide range of organisations and individuals working in similar or related areas, both in the UK and globally (including, for example, in the US, the Netherlands and Malaysia) and from within and outside the banking sector.

The assessment work in 2016 and beyond will be multi-disciplinary and innovative. It will also be firmly rooted in identifying what is evidence-based, relevant and of practical application. We will endeavour, over time, to make as much as is appropriate of our methodology and approach open-source in order to facilitate dialogue, invite challenge and contribute to improvement and progress elsewhere.

Some elements of the annual assessment exercise will vary, year on year. There may, for example, be particular themes we wish to examine at any one time (such as the role of Remuneration Committees, or challenge and speaking up). It is also important that the approach used for the assessment does not become over-familiar or vulnerable to being gamed. We need, therefore, to strike the right balance between 'core' questions and techniques, and topical or themed elements. We will also, over subsequent assessment cycles, pilot new elements with individual firms that may or may not then be extended across the whole set of firms being assessed.

The assessment cycle in 2016 and in future years has naturally begun by drawing on as much relevant recent work and research as possible to ensure that whatever the BSB subsequently does is genuinely additive and fully informed. This encompasses the BSB's own previous findings, work undertaken by firms themselves, and research and analysis from a range of sources including (but not confined to):

- academic research on culture and behaviour;
- reports on culture in the financial services sector by other organisations;
- relevant publicly available data on banks and building societies (eg, complaints data);
- case studies of conduct failure and poor practice;
- lessons and experience drawn from other sectors;
- lessons and experience drawn from outside the UK; and
- existing culture tools and benchmarks.

Building on existing knowledge, core elements of the assessment exercise will then include:

- a short set of questions to boards and senior management teams about their perspectives on progress over the past year, the challenges and priorities for the coming year, and the information they are using to identify these challenges and measure progress;
- in-depth interviews with individual non-executive board members, in particular, with the heads of Remuneration Committees and committees that have responsibility for culture, conduct, values, reputation or similar;
- focused surveys of staff, not to duplicate what firms may already be doing in their own and often extensive staff engagement, but to test on a consistent basis across firms the efficacy of the 'tone from the top' and the alignment of views and practices across the organisation, and to identify both good practice and progress, and any emerging concerns or issues, with a view to facilitating systematic benchmarking across member firms and within peer groups; and
- qualitative exercises with staff such as focus groups, interviews and message boards to provide a deeper understanding of issues addressed or raised in the survey.

These core elements may then be combined, subject to whatever is relevant to the issues at hand or the institutions involved, with, for example:

- techniques drawn from a mixture of disciplines including, where relevant, ethnography, sociology, psychology or neuro-science to provide new and different perspectives on longstanding issues; and
- feedback and views from those the bank or building society engages with, eg, customers, investors, members, clients, regulators and prospective employees (eg, students).

The focus for 2016 will be on getting the core elements of the assessment exercise – the foundation for future years – right, in terms of both design and implementation. We will, nevertheless, deploy a range of different techniques in developing this core approach, and trial or introduce new elements where possible or where firms have a particular interest in an approach, with a view to their potentially wider subsequent application.

As noted, not all BSB member firms in any one year will participate in the assessment exercise. Smaller member firms have the choice to opt in, and branches of overseas firms are not eligible for practical reasons. We intend, however, to extend the survey element of the assessment exercise to all BSB members, including branches, in order to provide all firms with the ability to benchmark themselves against the sector and their peers, and to gain as broad a view as possible of developments across the sector.

Professionalism

The Parliamentary Commission on Banking Standards found that 'banking culture has all too often been characterised by an absence of any sense of duty to the customer and a similar absence of collective responsibility to uphold the reputation of the industry[9]', and argued that a greater focus on professionalism could be an answer to this. In parallel, a much commented-on feature of the banking sector in our own engagement with firms and other bodies has been the perceived decline in the acquisition of specific, banking-related professional qualifications among people who work in the sector, and the contrast with eg, accountancy or legal services that have accepted professional qualifications and professional bodies.

The question of whether banking is a profession is of course a matter for debate. Some would argue that it comprises several professions; others, none. It is also clear that the knowledge and skill required on a trading desk will differ in many respects from that required in corporate finance, and that this will be different again in other parts of the sector. While technical skills and understanding may differ, however, there may be core competences, aspects of behaviour and values that all staff working in the sector might be expected to share. That people working in banking should behave 'professionally' is, perhaps, rather less contentious than an assertion that banking is a 'profession' as traditionally defined.

We are interested in whether a more 'professional' approach to banking would improve behaviour and competence across the industry. Furthermore, given that two of the themes from the 2015 assessment exercise related to feeling confident about challenging and speaking up and having sufficient time, support and guidance for continuing professional development, we are also interested in exploring the appetite among members firms and professional bodies for enhancing the scale, scope and activities of such bodies in line with those found in professions such as medicine, engineering and accountancy, and whether such an approach could be beneficial in a banking sector context.

To answer this question and arrive at evidence-based, useful and useable recommendations, the BSB is working with a team at the University of Leeds to investigate how professional qualifications are currently used across the sector; if this is changing with the onset of the Senior Managers and Certification Regime[10]; if and how this would be affected if the qualifications on offer were any different; and whether there is merit, from the perspective of firms, in a stronger role for professional bodies in banking.

The project involves surveying and interviewing, in this context, banks and building societies, professional bodies and a wide range of other interested groups. This evidence-gathering exercise should be completed during the second quarter of 2016, at which point we will engage with firms, professional bodies and other interested parties on the findings and next steps.

We have also been considering how the broader issues of professionalism interact with the new Certification Regime (part of the comprehensive framework of regulatory change coming into effect this year and intended to ensure better accountability, professionalism and responsibility for behaviour, competence and culture in banks and building societies). Of particular interest is whether a common approach across firms could support both the objectives of the regime and the skills and development of the people covered by it.

We have, to this end, been working with member banks and building societies to develop a common understanding of the policy and operational issues associated with Certification, to identify examples of good practice, and to ascertain areas where a common approach across firms might be advantageous. These latter areas might include: addressing issues associated with employees who move between organisations; issuing regulatory references when staff move between firms; and dealing with overseas employees. This work, initiated via a working group in January 2016, is ongoing and will report to members in the second quarter of 2016.

[9] http://www.parliament.uk/documents/banking-commission/Banking-final-report-volume-i.pdf (excerpt from paragraph 19).

[10] https://www.the-fca.org.uk/improving-individual-accountability and http://www.bankofengland.co.uk/pra/Pages/supervision/strengtheningacc/default.aspx

Law, regulation and ethics

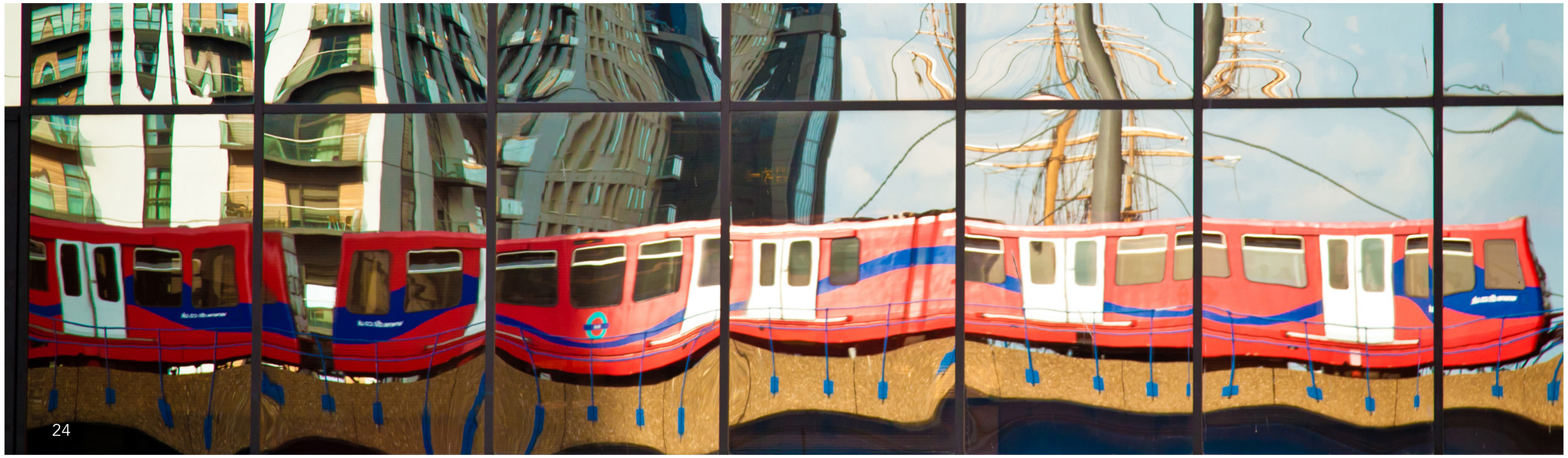
Compliance with the rules and standards prescribed by legislation or regulation is, in banking as elsewhere, one way of securing acceptable practice and conduct, but cannot of itself be sufficient. Legislation and regulation will always be incomplete; they will not achieve their aims unless those being regulated also respect and live up to more generic standards, and do not view legal or regulatory constraints as formalities or something to be gamed. These generic standards will encompass both ethical standards (for example, honesty, trustworthiness, fairness) and professional standards (such as competence, understanding and reliability). The extent to which firms and the industry as a whole meet these standards is a function less of regulation than of individual character and institutional practice and culture.

The balance between law, regulation and ethics is an important one. It is also a variable one. There is a saying that 'ethics begins where law ends', but the handover point is not fixed; when trust in the banking sector's ability to manage itself and maintain high ethical standards declines – as in the financial crisis – regulation (legal discipline) will naturally move in to fill the gap that is seen to have been vacated by ethics (institutional self-discipline).

Effective, proportionate regulation is vital for well-functioning markets and societies. In the area of culture, behaviour and competence, however, regulation can only go so far. While conduct can be regulated, there is no 'good' culture that can be mandated, and regulation cannot compel someone to behave professionally. Culture, behaviour and competence are the responsibility not of the regulator but of each individual firm, or more specifically of the board of each firm and the executive team. In addition, it is the collective responsibility of the industry as a whole to demonstrate that it is managing itself in this regard, and to maintain trust in its ability to do so. Without which a vacuum will be created that regulation will then be asked to fill.

Working with Queen Mary University of London's Centre for Regulation and Ethics and with members of the judiciary, we have begun to study how standards of behaviour and competence in the UK banking industry are set and shaped by law, regulation, codes and other standards, and to ask whether this balance is working effectively, and what this might imply for the industry. This is not a study devised to conclude that less regulation would be beneficial. It is, rather, asking what needs to be in place alongside regulation to produce the highest standards of behaviour and competence in banking; what is needed to fill the space beyond the 'boundaries of regulation', for that regulation to be not only bounded, but to work effectively. Its practical implications are therefore likely to be less about regulation *per se*, than about the gaps left around it, and the responsibility of the industry in filling that space.

This study is intended to have implications and benefits not only for the BSB's own work on professionalism and standards, but also across other sectors and jurisdictions. We will be continuing with this work during the first half of 2016, and reporting publicly on its conclusions later in the year.



Standards

The word 'standard' has been used frequently in this report, and the BSB is, as we have seen, committed to helping raise standards of both behaviour and competence across the banking sector. This can be done in a number of ways, including assessment and work on professionalism, but also by a commitment on the part of firms to reach a particular performance or service standard, to make this commitment public and to be accountable for it.

Identifying, developing and setting specific voluntary standards agreed with member firms, is part of the BSB's remit. With membership now open, we are exploring with member firms areas where such standards would be most effective in providing a better service and in raising aspirations and performance, taking into account existing standards, in all or part of the sector. Where potential areas are identified, we will consult with all relevant parties to ensure that, in line with good practice in standard-setting, the resulting standards add value and are fit for purpose. Questions as to how a firm is meeting an agreed standard will then be incorporated in the annual assessment process, and a verification mechanism established for firms not eligible for or not participating in the assessment exercise.

It is important that any standards issued by the BSB are implementable, properly targeted, and do not duplicate what already exists. Where a satisfactory voluntary standard is already in place or being developed, the BSB may support it or – if it currently only applies to part of the sector – consult on extending it across its membership. It will not, however, spend time and resource reinventing the wheel; and in a sometimes already crowded standard-setting space, we will seek always to simplify rather than complicate matters, for firms and customers alike.

BSB standards themselves will need to be stretching, positive and aspirational. They should not be simply a statement of current practice. They will also need to be clearly differentiated from minimum regulatory requirements. A voluntary standard – as we are exploring in our work on law, regulation and ethics – is not a regulation by another name. Standards play a different and complementary role to that of regulation. They may also need to change over time, to ensure that they remain useful to customers. BSB standards, once agreed, will be kept under review to ensure that they remain relevant, visible and ambitious.

Some of the BSB's existing work areas, especially on professionalism, may themselves suggest issues on which specific voluntary standards would be helpful. Another potential area is that of the relationship between banks and small and medium-sized enterprises (SMEs), characterised in recent years by some high profile instances of customer detriment, and where not all dealings of banks (or other authorised firms) with SMEs are regulated[11]. The Financial Conduct Authority (FCA) invited views in November 2015 on the way in which SMEs that use financial services are treated under FCA rules, and asked whether – among a number of options – voluntary codes and standards might be helpful in raising the level and consistency of service provided to SMEs[12]. The scope for standards to have a beneficial impact on the banking sector's relationship with SMEs will be considered by the BSB as it prioritises its work on standard-setting over the coming year.

[11] www.fca.org.uk/your-fca/documents/discussion-papers/dp15-07
[12] *ibid.*

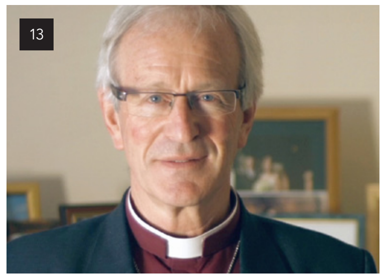
THE WAY FORWARD

The BSB has come a long way in a very short space of time. It has also, however, a long way to go and – as its ambitious agenda for 2016 demonstrates – no time to waste. The publication of this first annual review marks an important public milestone, but one that serves to put into even clearer perspective the distance still to travel.

It is not the BSB that will raise standards in the UK banking industry. Only the industry itself can do that. The responsibility for and ownership of culture cannot be delegated to the BSB, the regulator or anyone else; but where firms are committed to raising standards across the sector (and joining the BSB is a public statement by member firms of just such a commitment), the BSB can and will provide challenge and support that will help them achieve this.

A trustworthy UK banking sector will be one in which those working in banks and building societies in the UK can say not only that they are proud to work for their own firm (as many already are), but that they are proud to work in the banking sector. And the industry should set the bar higher still; it should aspire to ensure that the UK can be proud of its banking sector. This is clearly not going to happen quickly, and some might be sceptical of it occurring over any time horizon; but if – and only if – the industry is committed to making it happen, it can and it will. The industry's future is in its own hands.

ANNEX
THE BSB BOARD



1. **Chairman Dame Colette Bowe** has worked in the City, in regulation, and in Whitehall, and is former Chairman of Electra Private Equity and Ofcom.
2. **Deputy Chairman Sir Brendan Barber** is Chair of the Advisory, Conciliation and Arbitration Service (Acas). He is a member of the Board of Transport for London and of the Council of City University London and was the General Secretary of the TUC from 2003 to 2012.
3. **James Bardrick** is UK Head of Citi. James is a member of The CityUK Advisory Council, sits on the PRA Practitioner Panel and is also a Board member of the British Bankers' Association and British American Business.
4. **Craig Donaldson** is the Chief Executive Officer of Metro Bank. Prior to launching Metro Bank, Craig was the Managing Director of Retail Products and Direct Channels at RBS. He has also held senior roles at HBOS and at Barclays. Craig serves on the Board of Directors at TheCityUK.
5. **Gillian Guy** became Chief Executive of the independent charity Citizens Advice in July 2010. Gillian is currently Chair of the BBA Consumer Panel. Gillian is former CEO of the London Borough of Ealing, and CEO of Victim Support.
6. **Paul Johnson** is Director of the Institute for Fiscal Studies (IFS), and former Chief Economist at the Department for Education and Director of Public Spending in HM Treasury.
7. **Rt Hon John McFall, Lord McFall of Alcluith** was made a Peer in the 2010 Dissolution Honours List, following 23 years' service as the Member of Parliament for Dumbarton and later West Dunbartonshire. Lord McFall served as Deputy Chairman of the BSB from April 2015 to 31 January 2016.
8. **Saker Nusseibeh** is Chief Executive of Hermes, Chair of its Executive Committee and an Executive Board Director. He is former Global Head of Equities at Fortis Investments USA.
9. **Professor Onora O'Neill** Baroness O'Neill of Bengarve is an independent peer, Chairman of the UK's Equality and Human Rights Commission, and former Principal of Newnham College, Cambridge, and President of the British Academy.
10. **Lady (Susan) Rice CBE** was appointed Chair of Scottish Water on 1 June 2015. She is also Chair of the Scottish Fiscal Commission and a Non-Executive Director of Sainsbury's and the North American Income Trust. She was a member of the First Minister's Council of Economic Advisors, Managing Director of Lloyds Banking Group Scotland and was previously Chief Executive and then Chair of Lloyds TSB Scotland plc.
11. **Alison Robb** is a Group Director and member of the Executive Committee at Nationwide Building Society. She is a Chartered Accountant and qualified at KPMG before moving into business. She now leads a diverse team with accountability for human resources, communications, customer experience and commercial lending.
12. **António Simões** is the Chief Executive of HSBC Bank plc, with responsibility for the UK and Continental Europe. Previously, António was CEO for HSBC in the UK, and deputy Chief Executive of HSBC Bank plc.
13. **The Rt Revd David Urquhart Bishop of Birmingham** worked in commercial management with BP for ten years before studying theology at Oxford and becoming a parish priest. He is actively involved with education, industry and commerce.
14. **Clare Woodman** is Global Chief Operating Officer for Morgan Stanley's Institutional Securities Group and is a member of the firm's Global Operating & Management Committee. Clare is a Non-Executive Director of Euroclear, TheCityUK, GFMA and AFME (The Association for Financial Markets in Europe). Clare is a member of the Worshipful Company of International Bankers.
15. **Chief Executive Alison Cottrell** was previously Director of Financial Services at HM Treasury and began her career as an economist with firms including HSBC and PaineWebber.

Banking
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Board

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